No. 11155

In the United States Circuit Court of Appeals for the Ninth Circuit

GEORGE W. YOST, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

SEWALL KEY,
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OPINION BELOW

The only previous opinion in this case is the opinion of the Tax Court (R. 27–45), reported at 5 T. C. 140.

JURISDICTION

This appeal involves deficiencies in federal income tax assessed against George W. Yost, hereafter referred to as the taxpayer, for the years 1940 and 1941 in the respective amounts of $75.44 and $1,071.70. (R. 3–4, 28.) In a companion appeal to this Court by Juanita Yost, wife of the taxpayer, this Court has entered an order (R. 174–176) permitting the filing of an abbreviated record on appeal in the latter case, dis-

pensing with the printing thereof, and providing for the entry of judgment therein in accordance with the final decision in the instant case.

Under date of March 23, 1944, the Commissioner of Internal Revenue, pursuant to Section 272 (a) of the Internal Revenue Code, mailed a statutory notice of deficiency to the taxpayer proposing to assess against him the deficiencies shown above. (R. 16–21.) Within the time allowed therefor the taxpayer filed a petition with the Tax Court for review of the Commissioner's determination. (R. 3–16.) The Tax Court, after hearing in due course, entered its decision under date of May 28, 1945, affirming the Commissioner's determination. (R. 45–46.) Under date of August 24, 1945, the taxpayer filed with the Clerk of the Tax Court, pursuant to Sections 1141 and 1142 of the Internal Revenue Code, a petition for review by this Court of the decision entered by the Tax Court on August 24, 1945. (R. 161–173.)

QUESTION PRESENTED

Whether one-half of the net amounts of $2,603.65 and $12,799.99 received by the taxpayer and his wife in 1940 and 1941, respectively, from Richard B. Newell and Robert L. Newell pursuant to certain agreements shown by the record constituted ordinary income of the taxpayer within the meaning of Section 22 (a) of the Internal Revenue Code or constituted long-term capital gain from the sale or exchange of capital assets within the meaning of Section 117 (a) of the Code.

STATUTE INVOLVED

Internal Revenue Code:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

(26 U. S. C. 1940 ed., Sec. 22.)

SEC. 117. CAPITAL GAINS AND LOSSES.

(a) *Definitions.*—As used in this chapter—

(1) *Capital assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would probably be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l);

(2) *Short-term capital gain.* — The term "short-term capital gain" means gain from the sale or exchange of a capital asset held for not

more than 18 months, if and to the extent such gain is taken into account in computing net income;

* * * * *

(4) *Long-term capital gain.*—The term long-term capital gain'' means gain from the sale or exchange of a capital asset held for more than 18 months, if and to the extent such gain is taken into account in computing net income;

* * * * *

(b) *Percentage Taken Into Account.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:

100 per centum if the capital asset has been held for not more than 18 months;

66⅔ per centum if the capital asset has been held for more than 18 months but not for more than 24 months;

50 per centum if the capital asset has been held for more than 24 months.

* * * * *

(26 U. S. C. 1940 ed., Sec. 117.)

STATEMENT

This appeal involves deficiencies in federal income taxes asserted against the taxpayer for the years 1940 and 1941 in the respective amounts of $75.44 and $1,071.70. (R. 3–4, 28, 47.) At all times material to this proceeding the taxpayer and Juanita Yost were married and living together as husband and wife at Edmonds, Washington. They filed separate income

tax returns for the years involved with the Collector of Internal Revenue for the District of Washington, each reporting one-half of the community income. (R. 46, 151–159.) The Commissioner determined like deficiencies against each spouse as a result of the adjustments here involved and their separate appeals to the Tax Court were heard and decided together by that court. (R. 28, 46.) Separate appeals were taken from the Tax Court's decisions, but by order of this Court only the record in the taxpayer's case was printed, and the decision in this case will be controlling in the wife's appeal. (R. 174–176.) The deficiencies in both cases arise out of the same transactions and the only question involved is whether amounts received by the marital community in 1940 and 1941 from Richard B. Newell and Robert L. Newell, pursuant to certain agreements theretofore entered into between the parties, constituted ordinary income or capital gains from the sale of capital assets. (R. 28.) The cases were submitted to the Tax Court upon a stipulation of facts and documentary exhibits, plus oral testimony of the taxpayer and others. (R. 46–159.) The Tax Court sustained the Commissioner's determination (R. 27–46) and this appeal followed (R. 161–173).

For some time prior to the taxable years involved, the taxpayer had been, and still is, engaged in the bus passenger transportation business in suburban Seattle as part owner and general manager of Suburban Transportation System. For a number of years prior to 1935 Richard B. Newell had been a draftsman

and chief engineer for Heiser's, Inc., manufacturers of bus and truck bodies at Seattle, and Robert L. Newell had been engaged in the sale throughout the Pacific Northwest of bus and truck bodies manufactured by Wentworth and Irwin of Portland, Oregon. For some time prior to January 28, 1935, the Newells had discussed with the taxpayer the formation of a new company to manufacture bus and truck bodies. As a result they organized Tricoach Corporation, a Washington corporation with its principal office at Seattle, on January 28, 1935, with an authorized capitalization of $50,000 represented by 1,000 shares of $50 par value common stock. Thereafter, and at all times material here, these three individuals owned all of the outstanding stock of the corporation and were its only officers and directors. Robert Newell was president and sales manager. Richard Newell was vice-president and general sales manager. The taxpayer was secretary. The Newells each received an agreed monthly salary, and in addition thereto they and the taxpayer were each to receive adjusted compensation equal to one-third of the annual net profits of the corporation in excess of an amount necessary to pay eight per cent dividends on the outstanding stock. (R. 28–30, 47–49.)

Only a part of the stock of Tricoach Corporation was issued at the time of organization, but by the end of 1937 all of the stock was issued and outstanding. At that time the taxpayer owned 510 shares, fully paid, or 51 percent of the outstanding stock, which had a cost basis to him for tax purposes of $26,-

501.42, and the two Newells owned the balance of the stock in equal amounts. (R. 30–31, 38, 51, 53, 58.)

As of November 1, 1937, the taxpayer and the two Newells formed a partnership under the name of Tricoach Sales Company to carry on the general business activities pertaining to the wholesale and retail distribution of motor vehicles and trading in commercial paper relating to such transactions. The taxpayer contributed $20,000 and had a 50 percent interest, while the Newells contributed $10,000 each and each had a 25 percent interest. (R. 31–32.)

In March, 1936, Heiser's, Inc. (former employer of Richard Newell), made an assignment for benefit of creditors and during 1936 all of its machinery and equipment was sold to Pacific Car and Foundry Company, was installed in the latter's Renton plant, and a bus body manufacturing plant was started in competition with Tricoach Corporation which resulted in considerable loss to Pacific Car and Foundry Company for 1936 and 1937. For several months in 1938, Pacific negotiated with the taxpayer and the Newells for the purpose of accomplishing a merger or consolidation, or working out of some method to eliminate the competition of Tricoach Corporation and to secure the services of the two Newells to manage the production and sales of the motor coach division of Pacific Car and Foundry Company. The arrangement finally worked out, which is reflected in agreements made a part of the record (pp. 80–115) and fully carried out contemplated leasing by Tricoach Corporation of its machinery and equipment to the

Newells for ten years, with an option to them to purchase it before December 31, 1938, at its depreciated book value; the Newells then were to sublease to Pacific Car and Foundry Company all of the Tricoach Corporation machinery and equipment for seven and one-half years from October 1, 1938, and it was to be moved at Pacific's expense to the Renton plant. Pacific was to operate its motor coach division for seven and one-half years from October 1, 1938; to employ the Newells for that period at a minimum salary of $250 per month each and, in addition thereto, to pay each of the Newells one-sixth of the profits of the business of the motor coach division earned during the term of the agreement; and Pacific was to purchase, as needed, for cash at then market prices, all of Tricoach Corporation's materials inventory. (R. 32–33.)

This master agreement (R. 80–104), signed by all the parties (R. 104), and frequently referred to in the opinion of the Tax Court as the four-party agreement, was executed August 3, 1938. At the same time the taxpayer and each of the Newells entered into identical separate subsidiary agreements (R. 104–111) which recited, among other things, that (R. 105, 108–109):

> In Consideration that the second party [the taxpayer] shall consent to and enter into a certain contract between the Pacific Car and Foundry Company, a corporation, the Tricoach Corporation, a corporation, et al, * * * [the four-party agreement] and shall, on or before December 31, 1938, advance to first party the sum of Forty-one Hundred Eighty-seven

> 83/100 ($4,187.83) Dollars, without interest, to be used by first party for the purpose of acquiring joint ownership of the machinery and equipment to be sub-leased to the Pacific Car and Foundry Company as set forth in * * * [the four-party agreement], the first party hereby agrees to pay unto second party an amount equivalent to;—
>
> one-third (⅓) of all compensation, or damages in lieu thereof, not in excess of Thirty-seven Thousand Five Hundred Dollars ($37,500.00), said first party shall receive or be entitled to receive from the Pacific Car and Foundry Company by reason of said contract as set forth in Exhibit "A" attached, exclusive of the minimum salary of $250.00 per month and rental income separately set forth in said contract.
>
> Payments to be made within three (3) days after first party shall receive an accounting and settlement of his adjusted bonus compensation from the Pacific Car and Foundry Company for each respective calendar year or fractional period.

Each agreement between the taxpayer and the Newells further provided that, in the event that all or any part of the machinery and equipment involved should be sold by the Newells, one-fourth of the net proceeds derived from the sale should be paid to the taxpayer and applied in liquidation of the $4,187.83 loan, and that one-half of all other payments made pursuant to the agreement would be applied in liquidation of the loan until it should be paid in full. In the event that either (Richard or Robert) should

terminate his employment with Pacific Car and Foundry Company, either voluntarily or by death, the unpaid balance was to become due and payable with an option in the first party or his legal representatives to assign to the taxpayer an undivided one-fourth interest in the machinery and equipment, together with the proportionate share of rental income to be subsequently earned. In the event the named Newell should continue in the employ of Pacific for the full seven and one-half years, then the taxpayer agreed to waive and forgive any unpaid balance on the loan of $4,187.83. (R. 34–35, 104–111.)

At a joint meeting of stockholders and directors of Tricoach Corporation held on August 2, 1938, the day preceding execution of the above agreements, a resolution was adopted to suspend the manufacturing operations of the corporation on or about October 1, 1938; to gradually liquidate its affairs; to enter into the proposed agreement with Pacific (the four-party agreement); and to enter into a lease agreement with the Newells for lease of the corporation's manufacturing machinery and equipment with an option in them to purchase on or before December 31, 1938, for cash at the depreciated book value. An agreement, signed by all of the stockholders of Tricoach Corporation under date of August 2, 1938, restricting the sale or transfer of shares of stock of the corporation to persons other than the present stockholders or members of their families, was received and filed as an appendix to the minutes of this joint meeting. (R. 35–37, 111–115.)

On June 26 1940, the taxpayer received $25,500 (an amount equal to the par value thereof) from Tricoach Corporation and signed a receipt stating in part (R. 38, 116):

> In event the Tricoach Corporation shall resume its business activities the undersigned hereby agrees to return the funds thus advanced; but, if business activities are not resumed, the funds thus advanced shall, upon dissolution, be applied in settlement of any liquidating dividends that may be declared.

There is nothing in the record to show that Tricoach Corporation ever was liquidated, or that the taxpayer ever surrendered or transferred his 510 shares of stock therein. In fact, the contrary appears to be true. As stated above, the taxpayer's 510 shares of stock had a cost basis, for income tax purposes, of $26,501.42, and the Commissioner in determining deficiencies against the taxpayer and his wife for 1940, allowed as a deduction to each for a long-term capital loss one-half of the difference on the theory that the $25,500 received from the corporation represented a liquidating dividend. (R. 38.)

In 1940 the taxpayer received from the Newells, under the agreements mentioned above, the net sum of $2,603.65 after deduction of the amounts applied on loans to them, and in 1941 he received the net sum of $12,799.99 (reflected as $12,800 in the returns (R. 156, 158) and deficiency notices (R. 21)) after deduction of the balance of the loans to them, which amounts the taxpayer and his wife reported as gain upon the sale or exchange of capital assets held for more than 18

months and therefore only one-half of which was includible in gross income for federal income tax purposes. In auditing their returns for the years involved, the Commissioner treated those amounts as ordinary income taxable in its entirety to the two spouses, and in his notices of deficiency explained that the amounts in question were not received from the sale or exchange of capital assets as defined by Section 117 of the Internal Revenue Code, and were not distributed by a corporation in cancelation or redemption of all of its capital stock in accordance with a plan of liquidation, as contemplated by Section 115 (c) of the Internal Revenue Code. (R. 18, 21.) The Tax Court sustained the Commissioner's determination. (R. 27–45.)

SUMMARY OF ARGUMENT

The taxpayer and his two associates owned all of the stock in Tricoach Corporation. His two associates contracted to give their services to a competing concern under an arrangement, agreed to by the taxpayer, under which the taxpayer financed the sale of Tricoach Corporation's machinery and equipment to the competing concern, he and Tricoach Corporation agreed not to engage in competition for the term of the arrangement, and in return he was to receive repayment of the loans advanced plus an agreed share of the profits to be earned by his associates under the new arrangement. The amounts received by the taxpayer under this arrangement constituted income for the years here involved. The amounts involved did not represent payments for the sale or exchange of

capital assets within the meaning of the Internal Revenue Code. The taxpayer did not sell or exchange his stock in the Tricoach Corporation. The payments received by him from his former associates, over and above the repayment of amounts loaned to them by the taxpayer, represented his share in the profits of the new undertaking and were taxable as ordinary income rather than capital gains.

ARGUMENT

The Tax Court did not err in holding that the amounts received by the taxpayer under the facts of this case constituted ordinary income rather than capital gain

The Internal Revenue Code imposes a tax at specified rates upon the net income of every individual for the years here involved. "Net income," for purposes of the tax, is defined by Section 21 of the Code as the gross income computed under Section 22, less the deductions allowed by Section 23. Section 22 (a) of the Code, *supra*, defines gross income to include "gains or profits and income derived from any source whatever." Certain exceptions are made by the statute for income derived from specified sources or under specified circumstances. In this case the taxpayer is relying upon the exception contained in Section 117 of the Code, *supra*. That section, after defining "capital assets," "long-term capital gain," and other terms pertinent to the computation of tax liability involving gains or losses realized upon the sale or exchange of "capital assets," provides, in so far as material here, that if a capital asset has been held for more than 24 months, only 50 per centum of the gain upon the sale

or exchange thereof shall be taken into account in computing net income.

In this case there is no disagreement over the amount of income or gain received by the marital community during the years involved, and there is no question that the capital asset—if it should be held that the profit involved was realized from the sale or exchange of a capital asset—was held for more than two years.

The whole burden of the taxpayer's contention in this case is stated in the headnote to his argument (Br. 12), where he asserts that the amounts involved were "Amounts Derived from the Sale or Exchange of Capital Assets and thus Constituted Long-Term Capital Gains to the Marital Community." The premise would be sound if substantiated by the facts. But the first paragraph of the taxpayer's argument (Br. 12) dispels any illusion as to the correctness of his position. He states that the sole question in the case is whether the net amounts received from the Newells during the years involved, "the main consideration for which was" (Br. 12):

> In consideration that the second party [Yost] shall consent to and enter into a certain contract between the Pacific Car and Foundry Company, a corporation, Tricoach Corporation, a corporation, *et al*, a copy of which is attached hereto and marked "Exhibit A" * * *

were capital gains as contended by the taxpayer, or ordinary income as held by the Commissioner and the Tax Court.

The rest of the argument (Br. 13–28) is anti-climax because the above statement of the question involved is in itself an admission that the amounts involved were not received by the taxpayer in connection with the sale or exchange of a "capital asset" as that term is defined in the Internal Revenue Code. Furthermore, it is difficult to ascertain from the argument as a whole just what the taxpayer considers the "capital asset" which was sold or exchanged.

At the outset the taxpayer asserts that his shares of stock in Tricoach Corporation represented two elements of value—51 per cent of the value of net tangible assets of the corporation and 51 per cent of the intangible or going concern value of its business. (Br. 13–14.) He apparently admits that the distribution of $25,500 received from the corporation in 1940 represents the net value of the tangible assets (Br. 17–19), and presumably contends that the amounts received from the Newells was in payment for the intangible value of the assets of the corporation. The Tax Court aptly labels this argument as "ingenious but unsound." (R. 41.) There is no evidence in the record to show what value, if any, the intangible assets of the corporation had. But what is more important, it seems to be well settled that intangibles, such as good will, are incidental to the business from which they grew and cannot be severed or carved out of the net value of the business and disposed of independently of the business as a going concern. In *Metropolitan Bank* v. *St. Louis Dispatch Co.*, 149 U. S. 436, 446, the Supreme Court said that undoubtedly good

will is in many cases a valuable thing, although there is difficulty in deciding accurately what is included under the term, but that it is tangible only as an incident connected with a going concern or business having a locality or name, "and is not susceptible of being disposed of separately." Compare *Pfleghar Hardware Specialty Co.* v. *Blair*, 30 F. 2d 614 (C. C. A. 2d); *Betts* v. *United States*, 62 C. Cls. 1, certiorari denied, 273 U. S. 762; *Washburn* v. *National Wall-Paper Co.,* 81 Fed. 17, 20 (C. C. A. 2d). In *Dodge Brothers* v. *United States,* 118 F. 2d 95, the Circuit Court of Appeals for the Fourth Circuit said (p. 100):

> Good will cannot be carved out of a business and sold independently of the going concern; for its tangibility and its value exist only to the extent that such tangibility and such value are connected with a going business.

In this case neither Pacific Car and Foundry Company nor the Newells acquired the right to use the name or place of business of Tricoach Corporation. The machinery and equipment was first leased to the Newells, and later sold to them, and was removed from Seattle to the Renton plant where it was installed as a part of the equipment of the motor coach division of Pacific. It thereby definitely lost its identity as machinery and equipment of Tricoach Corporation. Obviously no good will or other intangible value of the business of Tricoach Corporation was transferred to or followed the machinery to Renton. The principal intangible thing, if it can be so termed, which Pacific Car and Foundry Company or the Newells received from the taxpayer and

Tricoach Corporation was their agreement not to compete during the term of the four-party agreement. Finally, since this arrangement with Pacific Car and Foundry Company was only for a limited period, and since the corporate existence of Tricoach Corporation was maintained, it would be preposterous to say that the latter had sold its good will.

In this connection it should be noted that amounts received as compensation for agreements to refrain from competition under such circumstances are taxable as ordinary income rather than as capital gains. In *Salvage* v. *Commissioner*, 76 F. 2d 112 (C. C. A. 2d), affirmed, 297 U. S. 106, the court held that payment for a covenant not to engage in a competing business was income. In discussing this point the court stated (pp. 113–114):

> The contract under which the petitioner purchased the 1,500 shares of Viscose stock stated that the consideration for selling it at less than its real value was the petitioner's covenants relating to the option and to his refraining from engaging in a competing business. Compensation paid for refraining from labor would seem to be taxable income no less than compensation for services to be performed. For example, a farmer who is paid for voluntarily refraining from raising hogs receives, in our opinion, income. Certainly it is neither a captal payment nor a gift. The statutory definition of gross income is exceedingly broad. Section 213, Revenue Act 1921 (42 Stat. 237). We cannot avoid the conclusion that a payment for a covenant not to engage in a certain busi-

ness should be deemed "income" of the recipient of the payment.

In *Beals' Estate* v. *Commissioner,* 82 F. 2d 268 (C. C. A. 2d), affirming 31 B. T. A. 966, the court held that the value of stock received by the taxpayers in exchange for their several agreements not to engage in a competing business constituted income. As an alternative, the taxpayers there contended that the shares were received in exchange for property (presumably their right to engage in business), and that the gain realized upon the transaction should be taxed upon disposition of the capital asset. This contention was rejected, the court pointing out that even if the right to engage in business be considered property, it was not disposed of in exchange for stock. See also *Cox* v. *Helvering,* 71 F. 2d 987 (App. D. C.), in which the court held that the amount paid by the purchaser of a corporate business for the agreement of the stockholders to refrain from entering a competing business for a limited period constituted taxable income whether paid to the corporation or its principal stockholder, and *Estate of Hyde* v. *Commissioner,* 42 B. T. A. 738, where it was held that an amount paid to the decedent under an agreement which, among other things, contained her covenant not to enter into business in competition with certain corporations constituted ordinary income.

The taxpayer admits that the amounts received from the Newells for the years here involved were not received in exchange for his Tricoach Corporation stock. In fact, he makes a special point of the fact that the

payment of $25,500 from Tricoach Corporation in 1940 was all he received as a liquidating dividend on his stock. (Br. 17–19.) The reason for this argument is clear. Under the provisions of section 115 (c) of the Internal Revenue Code applicable to the years here involved, the gain derived from a liquidating dividend was to be treated as a short-term capital gain—or ordinary income—unless the distribution was a distribution in "complete liquidation" pursuant to a plan which required liquidation to be completed within a period of three years. The arrangement under which the taxpayer received the payments here involved did not satisfy this three year requirement so the amounts received from the Newells necessarily would have to be taxed as ordinary income if considered as a part of the distribution by the corporation in complete liquidation of its stock.

There may be some question whether the $25,500 received from Tricoach Corporation in 1940 actually constituted a liquidating dividend inasmuch as the corporation was not dissolved and the taxpayer continued to hold his stock. This question, however, is not involved in this case. But the taxpayer's admission that the only liquidating dividend he received was the $25,500 received from the company emphasizes the fact that the amounts received from the Newells were not received as payment for the sale or exchange of a capital asset.

The taxpayer relies entirely upon one decision of the Board of Tax Appeals and one decision of the Tax Court (Br. 20–25), neither of which is remotely ap-

plicable to the case at bar, and both of which were distinguished by the Tax Court in its opinion (R. 42–43). In both cases the payments in question clearly were made for a capital asset. But in this case the taxpayer has failed to point to a capital asset which he parted with as consideration for the payments received from the Newells. On the other hand, it is clear from the record as a whole that he insisted upon receiving a share in the Pacific Car and Foundry Company profits to be realized by the Newells because he had advance funds for them to finance the venture, had agreed to not engage in competition during the period of their agreement with Pacific, and was foregoing all possibility of realizing profit in the future from business operations by Tricoach Corporation, of which he held a majority of the stock. His insistence upon this arrangement where he could participate in the profits of Pacific Car and Foundry Company is both understandable and reasonable under the circumstances. But this does not make the payments received as a result of this new arrangement capital gains. They are not payments received for the sale or exchange of capital assets.

The taxpayer takes the position that the arrangement under which he received the amounts here involved was for all practical purposes the same as if he had sold his Tricoach Corporation stock for its par value and as an inducement for such sale the Newells had agreed to pay the additional amounts here involved. (Br. 25.) Thus he seeks to show the case is similar to *DeLong* v. *Commissioner,* 43 B. T. A. 1185.

No doubt the taxpayer insisted upon this additional amount because he felt that his stock in Tricoach Corporation, plus the amounts advanced to the Newells, was worth more than he could hope to collect upon liquidation of Tricoach Corporation. But his tax liability for the years involved must be determined upon the basis of what actually was done, not what he could have done. He did not part with his Tricoach Corporation stock, and the evidence indicates that he wanted to retain this stock as well as preserve the corporation because of the possibility of resuming the business operations of the corporation if the arrangement with the Newells and Pacific Car and Foundry Company should be abandoned or prove unprofitable.

Finally, the taxpayer takes exception to that part of the Tax Court's opinion (R. 45) classifying the payments received from the Newells in 1940 and 1941 as the fruits of a joint venture (Br. 25–28). But the Tax Court's characterization of the payments is correct. It is true that the taxpayer did not acquire any direct interest in either the stock or the assets of Pacific Car and Foundry Company. But he advanced the money needed by the Newells to purchase the machinery and equipment of Tricoach Corporation, he agreed to refrain from competition during the period of their agreement with Pacific Car and Foundry Company, and in return he was to receive from each the amounts agreed upon. His active participation in the venture was not necessary to make the arrangement a joint venture. Furthermore, the situation is not changed by the fact that the taxpayer entered into

a separate contract with each of the Newells instead of making it a three-party undertaking. Two parties can enter into a joint venture for their mutual profit and benefit. That was in fact the substance of the taxpayer's arrangement with each of the Newells.

CONCLUSION

The decision of the Tax Court is correct. It is supported by the facts and the law and should be affirmed.

Respectfully submitted,

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JANUARY, 1946.

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